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Message Text

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ACTION EUR-12

INFO OCT-01 EA-06 ISO-00 AID-05 CEA-01 CIAE-00 COME-00

EB-07 FRB-01 INR-05 IO-10 NEA-06 NSAE-00 RSC-01

OPIC-03 SP-02 TRSE-00 CIEP-01 LAB-04 SIL-01 SWF-01

OMB-01 AGR-05 SS-15 NSC-05 HEW-02 /095 W
---------- 103346
R 181915Z DEC 74
FM USMISSION OECD PARIS
TO SECSTATE WASH DC 4805
INFO AMEMBASSY BERN
AMEMBASSY BONN
AMEMBASSY BRUSSELS
AMEMBASSY COPENHAGEN
AMEMBASSY THE HAGUE
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PASS TREASURY AND CEA FOR SEEVERS

E.O.11652: N/A
TAGS: ECON, OECD
SUBJECT: EPC'S WP-4 MEETING ON PROBLEMS OF INFLATION,
DEC 5-6

REFS: (A) USOECD 29794
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(B) USOECD 26714

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1. SUMMARY: WP-4 AGREED IN GENERAL TERMS WITH SECRETARIAT FORECASTS OF ABOUT 11 PERCENT RATE OF INFLATION FOR OECD AREA IN 1975, AND NOTED PROSPECT OF SOME RELIEF AS COMMODITIES AND INDUSTRIAL RAW MATERIALS (AND HOPEFULLY FOOD) PRICES BEGIN TO STABILIZE. WAGE PRESSURES ARE NOW LIKELY TO BE GREATEST INFLATIONARY THREAT, AND MAIN PROBLEM OF GOVERNMENTS WILL BE TO ESTABLISH SUFFICIENT CONSENSUS ON RELATIVE BURDEN-SHARING OF SOCIAL GROUPS IN REACHING AIM OF CONTROLLING INFLATION. REDUCTION OF INFLATION RATE WILL BE COMPLICATED BY EXPECTATION THAT GOVERNMENTS WILL ACT TO PREVENT FURTHER SLACK IN ECONOMIES BEFORE ALLOWING RATE OF INFLATION TO RESPOND FULLY TO RESTRICTIVE DEMAND MANAGEMENT MEASURES. WP-4 AGREED TENTATIVELY WITH SECRETARIAT THAT ALL COUNTRIES WILL FIND IT USEFUL TO TAKE SELECTIVE MEASURES OF SOME SORT TO INFLUENCE WAGE AND PRICE DEVELOPMENTS, BUT DID NOT AGREE THAT FORMAL CONTROLS WOULD BE NEEDED. SECRETARIAT IS PREPARING CHAIRMAN'S SUMMARY OF MEETING WHICH WILL BE FORWARDED WHEN AVAILABLE IN FORM APPROVED BY CHAIRMAN. END SUMMARY.

2. OUTLOOK FOR PRICES: WP-4 AGREED THAT PROSPECTS FOR PRICES REMAIN UNSATISFACTORY FOR 1975, ALTHOUGH COUNTRIES WERE SLIGHTLY MORE OPTIMISTIC THAN SECRETARIAT REGARDING OUTLOOK. COUNTRY REPS ENVISAGED RISES IN CONSUMER PRICES OF ABOUT 11 PERCENT IN 1975 FOR OECD AREA, ABOUT ONE PERCENT LESS THAN SECRETARIAT ESTIMATE. SOME COUNTRIES (INCLUDING U.S.) FELT THAT SUBSTANTIAL MODERATION IN PRICE RISES MIGHT OCCUR IN SECOND HALF OF 1975 IN VIEW OF (A) MARKED DETERIORATION IN DEMAND CONDITIONS, (B) LEVELING OFF OF COMMODITY PRICES, (C) DECLINE IN INDUSTRIAL RAW MATERIAL PRICES, AND (D) IMPROVED FOOD SUPPLY PROSPECTS. WP-4 AGREED THAT WAGES HAVE BECOME PRIME MOVER OF INFLATION, AND SOME FELT THAT INFLATIONARY EXPECTATIONS AND EFFORTS TO CATCH UP ON RECENT REAL INCOME LOSSES MIGHT STIMULATE FURTHER SUBSTANTIAL WAGE CLAIMS.

3. LATEST ESTIMATES OF CPI AND GNP DEFLATORS WERE PRO-
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VIDED BY MOST COUNTRIES FOR 1974 AND 1975. THESE INCLUDE SOME CHANGES, NOTABLY FRANCE AND ITALY, FROM FORECASTS GIVEN AT SHORT-TERM FORECASTERS MEETING IN EARLY NOVEMBER (REF B). U.S. (SEEVERS) NOTED THAT BOTH CPI AND GNP DEFLATORS ARE EXPECTED TO BE BELOW SECRETARIAT ESTIMATES FOR 1975, WITH FINAL OUTCOME DEPENDING ON DURATION OF COOLING-OFF PERIOD IN U.S. ECONOMY. (FOR COMPARISON OF COUNTRY ESTIMATES GIVEN

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BELOW WITH SECRETARIAT ESTIMATES IN ECONOMIC OUTLOOK,
SEE REF A.) ALL FIGURES ARE PERCENTAGE CHANGES AT
ANNUAL RATES FROM PREVIOUS YEAR.

	CONSUMER PRICES		GNP DEFLATOR	
	1974	1975	1974	1975
CANADA	11	11	13	11
U.S.	11	NA	10	NA
JAPAN	24.5	13	23.75	13.75
FRANCE	13.8	10	9.2	9.7
GERMANY	7.1	6.5	6.1	6.5
ITALY	19	20	15.5	18
UK	NA	NA	NA	NA

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TO SECSTATE WASH DC 4806
INFO AMEMBASSY BERN
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4. IN ADDITION, ESTIMATES BY SMALLER COUNTRIES ARE GIVEN BELOW IN COMPARISON WITH SECRETARIAT FORECASTS FOR 1975 ONLY.

CONSUMER PRICES GNP DEFLATOR
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COUNTRY	SECT.	COUNTRY	SECT.
BELGIUM	11	11.5	10	10.5
NETHERLANDS	9.5	10.5	10.5	10.5
DENMARK	13	14.5	13	15
AUSTRIA	9.5	11	9	11
FINLAND	12.5	14	13	13.5
NORWAY	11	12	10	12.5
SWEDEN	10.8	11	10.3	11.5
SWITZERLAND	8.75	7.75	8.25	7.25
SPAIN	13-14	13	13	12.5

5. POLICY PROSPECTS: SECRETARIAT (ATKINSON) PAINTED BLEAK OUTLOOK FOR INFLATION PROSPECTS IN 1975 AND WAS PESSIMISTIC ABOUT POLICIES WHICH COUNTRIES MIGHT FOLLOW TO CONTAIN IT. EVEN WITH COUNTRIES MAINTAINING RESTRICTIVE DEMAND MANAGEMENT POLICIES FOR TWO-YEAR COOLING-OFF PERIOD, INFLATION RATE LIKELY TO REMAIN IN DOUBLE FIGURES FOR OECD AREA AS WHOLE FOR 1975. SECRETARIAT DOUBTED THAT COUNTRIES COULD CONTINUE TO MAINTAIN POLICY OF DEFLATION MUCH LONGER, WITH UNEMPLOYMENT PROSPECTS DETERIORATING AND PUBLIC PRESSURES BUILDING UP FOR REFLATIONARY ACTION. ONE DILEMMA FOR COUNTRIES WAS THAT WAGES MIGHT HAVE TO RISE SUFFICIENTLY TO MAINTAIN REAL INCOMES IF THERE IS TO BE CONSUMPTION TO SUPPORT DESIRED LEVEL OF GROWTH. YET SUCH WAGE INCREASES MAY BE TOO HIGH TO PERMIT EFFECTIVE CONTROL OF INFLATION. SECRETARIAT SOLUTION IS FOR GOVERNMENTS TO OFFER REAL INCOME INCREASES IN EXCHANGE FOR LOWER WAGE CLAIMS, BY USE OF SUBSIDIES, INDIRECT TAX CUTS, REDUCED FISCAL DRAG, DIRECT TAX REDUCTIONS AND OTHER MEASURES. BUT EVEN THIS MAY ONLY MAKE IT POSSIBLE TO CUT INFLATION

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RATE TO 10 OR 15 PERCENT PER ANNUM. THUS, SECRETARIAT ASKS RHETORICALLY WHETHER WAGE-PRICE FREEZE MAY NOT BE ONLY SOLUTION.

6. WP-4 AGREED WITH SECRETARIAT THAT SELECTIVE MEASURES MIGHT BE NECESSARY TO SUPPLEMENT DEMAND MANAGEMENT, BUT FEW COUNTRIES WERE WILLING TO ENDORSE A WAGE-PRICE FREEZE. U.S. (SEEVERS) NOTED THAT INFLATION RATE COULD BE 15-20 PERCENT OR 5-8 PERCENT DEPENDING ON POLICIES,
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AND COUNTRIES SHOULD NOT ABANDON DEMAND MANAGEMENT TOO PRECIPITOUSLY. HE NOTED THAT GERMANY HAD SUCCEEDED BETTER THAN MOST IN CONTAINING INFLATION BY USE OF DEMAND MANAGEMENT, AND HE DOUBTED THAT PRICE AND INCOME CONTROLS COULD HAVE MORE THAN TEMPORARY IMPACT ON INFLATION RATE. IN U.S. CASE, PRICE CONTROLS HAD SIMPLY PUSHED PROBLEM FORWARD AND HAD CREATED SUPPLY BOTTLENECKS WHICH THEMSELVES WERE INFLATIONARY. U.S. WAS NOT, HOWEVER, FOLLOWING PURELY "FRIEDMAN APPROACH" TO INFLATION CONTROL, SINCE WE HAD TRIED PRICE CONTROLS (UNSUCCESSFULLY) AND ALREADY HAD STATUTORY INDEXING OF FOOD STAMPS, SOCIAL SECURITY MEDICARE, AND FEDERAL PENSIONS AND VOLUNTARY INDEXING OF SOME WAGES AND FINANCIAL INSTRUMENTS. UK DELEGATE, WHILE TAKING OPPOSITE VIEW ON FEASIBILITY OF CONTINUED DEMAND RES-

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INFO AMEMBASSY BERN
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TRAINT, NEVERTHELESS AGREED THAT PRICE CONTROLS MIGHT
ONLY SUCCEED IN REDUCING INFLATION RATE BY 1-2 PERCENT.

7. SECRETARIAT (FAY) DESCRIBED HIS VIEWS ON INCOME
POLICIES AND PRICE AND WAGE CONTROLS BASED ON EXPERIENCE.
THESE WERE THAT COUNTRIES CANNOT HOPE FOR SUCCESS FROM
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SUCH POLICIES UNLESS THEY ARE COMBINED WITH APPROPRIATE
DEMAND MANAGEMENT. SELECTIVE POLICIES MUST BE APPLIED
FLEXIBLY AND WILL HAVE BEST CHANCE OF SUCCESS IN
CONDITIONS OF SLACK DEMAND ; IN TIME OF EXCESS DEMAND
THEY WILL BE SELF-DEFEATING.

8. CHAIRMAN (SLATER) SUMMED UP BY NOTING THAT EVEN
THOSE COUNTRIES WHO WERE PUTTING MAIN EMPHASIS ON DEMAND
MANAGEMENT WERE ALSO DOING SOME EXPERIMENTING WITH OTHER
APPROACHES. THERE IS DIFFERENCE OF VIEW REGARDING
EFFECTIVENESS OF SUCH OTHER MEASURES, BUT IN LIGHT OF
INFLATION RISKS AHEAD ALL COUNTRIES NEED TO THINK IN
CONTINGENCY TERMS AND CONTINUE TO SEARCH FOR SOLUTIONS.
MOST COUNTRIES DO NOT KNOW AT PRESENT HOW TO GET BELOW
TWO-DIGIT INFLATION, AT TIME WHEN INFLATIONARY EXPECTA-
TIONS ARE ALREADY BECOMING BUILT INTO SYSTEM (ESPECIALLY

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IN WAGE BARGAINING). THERE IS CLEAR NEED TO UNDERSTAND PROBLEM BETTER AND REACH AGREEMENT ON HOW BURDEN IS TO BE SHARED.

9. SLATER OF CANADA WHO ELECTED AS TEMPORARY CHAIRMAN OF WP-4 PUT IN MASTERFUL PERFORMANCE. IT APPEARS THAT HIS RESPONSIBILITIES IN OTTAWA MAY MAKE IT IMPOSSIBLE FOR HIM TO ASSUME POSITION WHEN WP-2 SELECTS ITS PERMANENT CHAIRMAN AT THE NEXT MEETING, WHICH SCHEDULED FOR EARLY MAY. THERE WAS LITTLE DISCUSSION OF THE AGENDA FOR THIS MEETING, WHICH WILL PROBABLY BE INFLUENCED BY INTERVENING EVENTS.
TURNER

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